

IRS



Fact Sheet

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2002 TAX CHANGES FOR BUSINESS TAXPAYERS

Fewer Tax Forms for Small Businesses to File

Starting with the 2002 tax year, companies with less than \$250,000 of total receipts and less than \$250,000 in assets no longer have to complete Schedules L, M-1 and M-2 of Form 1120; Parts III and IV of Form 1120-A; and Schedules L and M-1 of Form 1120S.

Small businesses will be able to use recordkeeping based on their checkbook or cash receipts and disbursements journal instead of creating additional records just for tax purposes. The companies must still maintain records detailing assets, liabilities, equity accounts and adjustments used to arrive at taxable income.

Self-Employed Health Insurance Deduction

Self-employed taxpayers generally may deduct 70% of their 2002 medical and long-term care insurance payments for themselves and their families as an adjustment to income. They may include the remaining costs with their other medical deductions if they itemize deductions. In 2003, they generally will be able to deduct the full cost of such insurance without itemizing deductions on Schedule A.

Special Depreciation Allowance

Businesses that acquire and begin using new qualified equipment after Sept. 10, 2001, may deduct an additional 30% of the depreciable basis in the first year of use. This Special Depreciation Allowance is figured after first reducing the basis by any Section 179 deduction taken. The allowance, in turn, is subtracted from that basis to determine the basis remaining for depreciation. This tax break will be available for property acquired before Sept. 11, 2004 and placed into service by the end of that year. Taxpayers may choose not to claim this allowance by attaching an appropriate statement to their tax returns.

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Section 179 Deduction Higher for Enterprise Zone and Renewal Community Businesses

The maximum Section 179 deduction for these businesses is increased by \$35,000 (to \$59,000) for 2002.

Five-Year Carryback of Net Operating Losses

Taxpayers with net operating losses (NOLs) for tax years ending in 2001 or 2002 will generally carry them back five years, rather than two (three, for certain casualty, theft and disaster-related losses). However, they may choose to use the two- or three-year period instead, or to carry the entire NOL forward for up to 20 years. Taxpayers waiving the five-year rule must do so by their filing deadline (including extensions).

Electric and Clean-Fuel Vehicles

The maximum amounts for the clean-fuel vehicle deduction and the electric vehicle credit, which were scheduled to begin dropping by 25% per year in 2002, will remain unchanged until 2004, when the three-year phaseout will begin.

Credit for Pension Plan Start-up Costs

This new tax credit helps small businesses offset the costs of setting up and administering a new qualified employer plan and educating employees about it. The credit is 50% of these costs, with a maximum amount of \$500 per year. After the first year the credit is claimed, it may be claimed again only in the following two years. To qualify, a business must have had no more than 100 employees who received at least \$5,000 in pay during the preceding year. The plan must include at least one non-highly compensated employee.

Credit for Employer-Provided Child Care

This new credit is 25% of the qualified expenses paid for employee child care, plus 10% of the qualified expenses paid for child care resource and referral services. The maximum credit amount is \$150,000 each year.

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Welfare-to-Work and Work Opportunity Credits

These credits, which were scheduled to end in 2001, have been extended to cover qualified wages paid to individuals who begin work before 2004.

New York Liberty Zone

Businesses in the Lower Manhattan area designated as the New York Liberty Zone have several tax breaks to aid in their recovery from the Sept. 11, 2001, terrorist attack. Among these are:

- A special Liberty Zone Allowance similar to the 30% Special Depreciation Allowance for property placed in service before 2007 that does not already qualify for that allowance. This includes used property that the taxpayer is the first to place in service in the Liberty Zone. Taxpayers may also elect not to claim this allowance.
- An additional Section 179 deduction of up to \$35,000, for a maximum amount of \$59,000. Generally, this limit is reduced by the cost of qualifying Section 179 property in excess of \$200,000. For Liberty Zone property, only 50% of the property's cost is taken into account when figuring this reduction.
- A new targeted group for the Work Opportunity Credit, consisting of new or existing employees who perform substantially all their services in the Liberty Zone, or elsewhere in New York City for a business that relocated from the Liberty Zone due to 9/11 attack damage.
- Classification of qualified Liberty Zone leasehold improvement property as 5-year property, for which the straight-line depreciation method must be used.
- Extension of the usual two-year replacement period for a tax-free replacement of involuntarily converted property to five years for Liberty Zone property converted as a result of the 9/11 attack.

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